EQUITY INVESTMENT CORPORATION

2018 Fourth Quarter Commentary
Mid-Cap Value
January 2019

Stocks fell for the fourth quarter and the full-year 2018. For the quarter, the Russell Midcap® Value Index (RMCV) dropped 15.0%. Our Mid-Cap Value (MCV) SMA composite decreased 10.5% (gross*). For the full year, the RMCV declined 12.3%. Our MCV SMA composite decreased 6.4% (gross*). Net of a 3% hypothetical maximum annual SMA fee, results for MCV would be -11.2% for the quarter and -9.2% for the year.[1]

Value beat growth for the first time in eight quarters. Though the Russell Midcap® Growth Index tumbled 16.0% during the quarter, that was not enough to offset its lead over value during the first nine months of the year. Accordingly, the Russell Midcap Growth Index declined 4.8% for the full year, surpassing its value counterpart (RMCV) by 7.5%.

In terms of size, large-cap outperformed mid-cap, which, in turn, outperformed small for both the quarter and the full year. More specifically, the Russell Top 200® Index fell 13.2% in the fourth quarter, and the Russell Midcap® Index decreased 15.4%. Meanwhile, the Russell 2000® Index dropped 20.2%, and the Russell Microcap® Index plunged 22.1%. For the year, the Russell Top 200 Index decreased 3.1%, and the Russell Midcap Index fell 9.1%. In the small-cap space, the Russell 2000 Index dropped 11.0%, while the Russell Microcap Index lost 13.1%.

Investment Environment

There were few places to hide last year. Aside from cash and some lower duration fixed income, not much worked for investors in the fourth quarter and full-year 2018. Domestic and international stocks declined, bond spreads widened significantly in both investment grade and high yield, and commodities broadly fell. Long-duration bonds and gold rose in the fourth quarter, but were down for the full year. In terms of breadth of the declines, 2018 was worse for investors than 2008. While the depth of the decreases in equities, commodities, and high yield was larger in 2008, investors were still able to make money in most categories of bonds and gold. Not so in 2018.[2]

Not one sector in the RMCV posted a positive return for the quarter. Utilities were the best performers at -1.4%, followed by real estate, down 6.4%, and consumer staples, down 10.4%. We were overweight consumer staples but underweight utilities and real estate, which is consistent with our historical allocations. While these three sectors have some defensive characteristics in terms of earnings stability and our holdings are justifiable on valuation, we don't view the group in aggregate as worthy of a significant overweight at this time. We think many constituents of these sectors have too much leverage, profitability or growth concerns, or trade at valuations that we view as unjustifiable.

Likewise, few stocks fared well. In fact, 93% of the names in the Russell 3000 Index fell 10% or more from their 2018 highs, 75% were down more than 20%, and 52% tumbled at least 30%.

Given this backdrop, it's not surprising that our value added relative to the RMCV was primarily attributable to our position in cash and short-term investments. Notably, cash is a residual of our stock selection process.[3]

2018 saw the return of market volatility, especially in the fourth quarter. At year-end 2017, the US equity markets received the gift of corporate tax reform, virtually ensuring strong 2018 earnings growth. Meanwhile, inflation remained tame, and unemployment hit historical lows. It was a Goldilocks scenario. In this context, the increase in volatility seemed to come out of left field.

Although volatility appeared elevated, it was actually closer to its historical average than to being an outlier. We believe 2018 volatility seemed much higher to many investors because of the contrast with preceding years. For instance, 2017 saw the lowest stock-market volatility in over half a century and marked the ninth consecutive year of positive S&P 500 performance, tying the previous record from 1991-1999.[2] 2017 was also the first time in EIC's 32-year history that the S&P 500 did not register a single down month during the year.

As we entered 2018, risks were mounting and bore similarities to previous periods of excess. Trading at 25x trailing GAAP and 23x Pro-Forma earnings, S&P 500 stocks were richly priced compared to historical levels.[4] And mid- and small-cap stocks looked even more expensive. Complicating matters, earnings were driven by historically high margins. Moreover, there was, in our view, significant complacency in corporate credit, with elevated leverage levels and lax underwriting standards. Short-term interest rates were rising, giving investors a safer and meaningful positive-return alternative to stocks for the first time in nearly a decade. And nine years into an economic expansion, the yield curve was beginning to flatten, signaling slower growth or worse ahead.

Today, corporate leverage and margins remain at historically high levels. The yield curve has flattened further. China's economic conditions softened during the year, along with US housing and some areas of technology. Finally, we have been living with trade-war rhetoric for much of the year. Investor's awareness of these risks is now higher than it was a year ago, and assets have repriced somewhat, particularly in the fourth quarter.

As a result of stock-price declines and earnings progress, valuations have improved. The S&P 500 began 2019 trading at 19x trailing GAAP and 17x Pro-Forma Earnings, still not cheap but a step in the right direction.[5] Moreover, despite the Q4 outperformance of value stocks, they remain inexpensive by historical standards relative to growth stocks. We believe starting valuation is an important determinant of forward returns. So while risks remain, we are pleased that prospects continue to broaden, giving us better opportunities to invest with expectations of reasonable returns.

Portfolio Review [6]

During the quarter, we purchased a new position in the Hartford Financial Services Group, a property and casualty insurance company focused primarily on commercial insurance. Hartford also has an employee benefits business offering group life and group disability coverages, as well as a mutual fund business. In 2018, Hartford sold the remainder of its individual life and variable annuity business, which had been a drag on company returns and a source of earnings volatility. Hartford's remaining businesses are of good quality and the sale should allow the better underlying fundamentals of these to prevail. The company is well capitalized and conservatively invested, and we believe the price we paid for the stock represents an attractive entry point that offers a degree of safety with upside potential.

Also during the quarter, we added to positions in KeyCorp, SunTrust and TCF Financial. Bank stocks declined reflecting, in part, increasing concerns about credit quality, and we took advantage of these better relative values.

As the market fell in the fourth quarter, especially in December, we harvested tax losses in a few positions and also added to several positions. In addition to the three banks noted above, we added to AmerisourceBergen, Encana and Mohawk, lowering cash and short-term investments in our representative account from approximately 36% at the beginning of the quarter to approximately 32% at December 31, consistent with our view that investment opportunities are improving.

As we enter 2019, we continue to be concerned about corporate leverage and the ability of companies to maintain historically high margins, given the expectations of slower growth ahead. Moreover, we think market volatility will likely persist this year, as investors digest the many forces impacting the economy, interest rates, and corporate profits. Nonetheless, our investment objective remains the same: constructing a portfolio of stocks that offers reasonable odds of investment success across a range of potential market outcomes.

Thank you for your continued partnership with EIC. We are grateful for the trust our clients have placed in us to manage a portion of their assets.

Investment Team

W. Andrew Bruner, CFA, CPA
R. Terrence Irrgang, CFA
Ian Zabor, CFA

Please see disclosures on the next page.

Disclosures

[1] EIC's MCV results are those of our Mid-Cap Value SMA composite gross (before) and net (after) assumed maximum annual SMA fees of 3% (0.25% per month). SMA fees include transaction costs, portfolio management, custody, and other administrative fees. *Gross returns for EIC SMA composites are "pure" gross returns, do not reflect the deduction of any expenses, including trading costs, and are presented as supplemental information to the full disclosure presentations which are considered an integral part of this report. All returns include reinvestment of dividends and interest. Indices are unmanaged, do not incur management fees, costs or expenses, and cannot be invested in directly. Past performance is not indicative of future results.* ***Individual account results may differ from those of a composite.***

[2] Bilello, Charlie, "2018: The Year in Charts." Pension Partners, 03 January 2019. https://pensionpartners.com/2018 -the-year-in-charts/. 15 January 2019.

*[3] Data Source: Morningstar Direct*SM

[4] Data Source: S&P Capital IQ. Trailing four quarters GAAP and Pro-Forma earnings as of September 30, 2017; Prices as of December 31, 2017.

[5] Data Source: S&P Capital IQ. Trailing four quarters GAAP and Pro-Forma earnings estimates as of September 30, 2018; Prices as of December 31, 2018.

[6] Portfolio data is from a representative Mid-Cap Value account. Actual portfolio holdings may vary for each client, and there is no guarantee that a particular client's account, "wrap," or advisory program will hold any, or all, of the securities identified. The securities identified and described above do not represent all of the securities purchased, sold or recommended for client accounts. The reader should not assume that an investment in the securities identified was or will be profitable.

S&P 500 and Russell indices are sourced from S&P Capital IQ.

Equity Investment Corporation (EIC) is an SEC registered independent investment advisor incorporated in the state of Georgia. EIC was founded in 1986. Effective September 30, 2016, substantially all of the assets and liabilities of the firm were acquired by three members of the investment team who collectively have more than 40 years of experience at EIC. Accounts continue to be managed using the same investment process, and the firm continues to operate as EIC. Performance numbers are the value-weighted, time-weighted, total return composite results of fully discretionary Mid-Cap Value wrap (SMA) accounts. The strategy invests in high-quality, well-managed mid-cap companies, while at the same time avoiding those that look inexpensive relative to their historical record but are actually in structural decline. Prior to January 1, 2013, the composite was called the Mid-Cap Value Wrap Composite. Returns are generally presented net of foreign withholding taxes on dividends, interest income, and capital gains; however, returns for some accounts are presented gross of foreign taxes depending on the treatment by their custodian. All accounts included in the composite are managed according to similar investment guidelines. The composite creation date is January 1, 2004, and SMA accounts comprise 100% of the composite. Performance includes reinvestment of dividends, and EIC's returns also include interest earned on cash. The benchmark index is the Russell Midcap® Value Index (which excludes an advisory fee), and was chosen because it is representative of the composite's investment style. The Russell Midcap® Value Index measures the performance of the mid-cap value segment of the US equity universe. It is a subset of the Russell Midcap® Index and includes approximately 800 of the Russell 1000® companies with lower price-to-book ratios and lower expected long-term mean earnings growth rates.

									Advisory-Only (UMA) and Managed Assets		
Year Ended Dec - 31	Gross* Rate of Return[1] (Supplemental)	Hypothetical 3% annual Net Rate of Return[1]	Benchmark Return of Russell Midcap® Value Index	Composite 3-Yr St Dev	Benchmark 3-Yr St Dev	Dispersion[2] of Annual Returns (St Dev)	Number of Portfolios	Composite Assets ($ Millions)	UMA Assets[3] ($ Millions) (Supplemental)	GIPS® Firm Assets ($ Millions)	Total Assets[3] ($ Millions) (Supplemental)
2018	-6.4%	-9.2%	-12.3%	8.4%	12.0%	0.7%	21	$4.7	$1,721.0	$2,219.9	$3,940.9
2017	12.6%	9.3%	13.3%	7.5%	10.3%	1.0%	20	$5.4	$2,044.9	$2,790.7	$4,835.6
2016	16.6%	13.2%	20.0%	8.4%	11.3%	1.0%	15	$4.3	$2,044.5	$2,994.4	$5,038.9
2015	-2.1%	-5.0%	-4.8%	8.9%	10.7%	1.0%	9	$2.3	$1,590.0	$3,658.9	$5,248.9
2014	15.2%	11.8%	14.8%	8.9%	9.8%	N/A	5	$1.8	$1,657.7	$3,862.6	$5,520.3
2013	33.6%	29.7%	33.5%	10.5%	13.7%	N/A	3	$1.1	$1,009.2	$3,286.3	$4,295.5
2012	11.3%	8.0%	18.5%	10.7%	16.8%	N/A	3	$0.9	$665.6	$2,301.1	$2,966.7
2011	5.3%	2.2%	-1.4%	15.3%	22.8%	N/A	1	$0.2	$314.5	$1,127.9	$1,442.5
2010	22.8%	19.3%	24.8%	17.9%	27.1%	0.4%	7	$1.7	$77.9	$836.9	$914.8
2009	28.1%	24.4%	34.2%	17.6%	25.0%	0.9%	8	$1.5	$10.5	$541.2	$551.8
2008	-20.4%	-22.8%	-38.4%	13.0%	18.7%	1.2%	11	$1.7	$0.0	$362.6	$362.6
2007	4.4%	1.3%	-1.4%	8.3%	9.1%	0.7%	16	$3.2	$0.0	$448.1	$448.1
2006	12.2%	8.9%	20.2%	7.3%	8.7%	0.5%	20	$6.6	$0.0	$487.2	$487.2
2005	6.0%	2.9%	12.7%	N/A	N/A	0.8%	29	$8.6	$0.0	$463.6	$463.6
2004	19.8%	16.3%	23.7%	N/A	N/A	N/A	32	$10.5	$0.0	$388.1	$388.1

[1] *Gross returns, presented as supplemental information, are "pure" gross and do not reflect the deduction of any expenses, including trading costs, for SMA accounts. Net returns are calculated by reducing gross returns with an annual SMA fee of 3.0% (0.25%/month).

[2] Dispersion is an asset-weighted standard deviation for the accounts in the composite the entire year (or year-to-date). "N/A" represents when dispersion is not statistically meaningful due to an insufficient number of portfolios in the composite for the entire year.

[3] "Total Assets" include our regulatory assets under management ("GIPS® Firm Assets") and our advisory-only "UMA Assets". EIC has no trading discretion for UMA accounts and provides a model portfolio to the program sponsor or overlay manager. The "UMA Assets" and "Total Assets" amounts are shown as supplemental information.

Additional Notes: The three year annualized standard deviation measures variability of the composite and the benchmark returns over the preceding 36 month period.

See next page for additional disclosures

Performance has been measured on a monthly basis from January 1, 2004, to present. Periods are geometrically linked to obtain the quarterly and annual results. Eligible new accounts are added to the composite at the beginning of the first full quarter under EIC management. Trade date accounting with monthly valuations and adjustments for large cash flows are used. Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. The US Dollar is the currency used to express performance. Returns include the reinvestment of all income. There are no non-fee paying accounts. Economic and market conditions have differed over the time period displayed, and likewise will be different in the future. Policies for valuing portfolios, calculating performance and preparing compliant presentations are available upon request.

EIC claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS® standards. EIC has been independently verified for the periods January 1, 1986, through September 30, 2018. Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS® standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS® standards. Verification does not ensure the accuracy of any specific composite presentation. The verification reports, as well as a complete list and description of all the firm's composites, are available upon request by contacting Equity Investment Corporation, 1776 Peachtree Street NW, Suite 600S, Atlanta, GA 30309. Prospective clients should be aware that results are historical and do not imply future rates of return or volatility for EIC or the indices, which may be materially different from the past and from each other.

Investment management fees are based on market values of the assets under management. In addition to a management fee, some accounts pay an all-inclusive fee based on a percentage of assets under management. Other than brokerage commissions, this fee includes portfolio monitoring, consulting services, and in some cases, custodial services. EIC's maximum annual fees for SMA accounts (charged quarterly) are 0.75%. Total fees charged may equal 3% per year. SMA schedules are provided by independent SMA sponsors and are available upon request from the individual sponsor. Further information about fees and compensation is discussed in EIC's form ADV Part 2 (www.adviserinfo.sec.gov).